

Message Text

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SUBJ: ECONOMIC AND DEVELOPMENT REVIEW COMMITTEE (EDRC) REVIEW
OF AUSTRALIA, MARCH 2, 1978

REF: (A) PARIS 7018, (B) EDR (78) 4 AND ADDENDUM

1. SUMMARY: EMBASSY AGREES WHOLEHEARTEDLY WITH MISSION
THINKING THAT REDISTRIBUTION OF FACTOR SHARES IN AUSTRALIAN
ECONOMY DOES NOT REQUIRE AS RESTRICTIVE AN ECONOMIC POLICY
AS IS BEING PURSUED. HOWEVER, EMBASSY BELIEVES FOREIGN
SECTOR CONSIDERABLY MORE COMPLEX THAN SUGGESTED BY MISSION'S
EMPLOYMENT/TRADE RESTRICTION FRAMEWORK, WITH NO EASY ANSWERS
IN SIGHT. END SUMMARY.

2. EDR REVIEW OF AUSTRALIAN ECONOMY CONTAINS AN IMPRESSIVE
AMOUNT OF SOUND ANALYSIS. HOWEVER, EMBASSY BELIEVES THAT
REVIEW MAY HAVE SOMEWHAT OVERLOOKED EXTRAORDINARY DEGREE OF
RESTRICTIVENESS IN AUSTRALIAN GOVERNMENT POLICIES.

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3. ALTHOUGH M3 TARGET FOR 1977/78 FINANCIAL YEAR IS 8-10
PERCENT, REALIZED GROWTH HAS BEEN WELL BELOW TARGET. IN
CY 1977 M3 GREW 5.9 PERCENT, WHILE M1 GREW 6.6 PERCENT.
THOUGH THESE FIGURES ARE APPROPRIATE FOR LONG-TERM. NON-
INFLATIONARY GROWTH, THEY ARE THE RESULT OF A VERY SHARP
WINDING DOWN OF MONEY SUPPLY GROWTH. MORE IMPORTANTLY, THEY
OCCUR IN CONTEXT OF CONTRACTIONARY FISCAL POLICY.

4. ANALYSIS BY A RESPECTED PRIVATE INSTITUTE SHOWS THAT FY 77/78 PLANNED BUDGET IMPLIES A SUBSTANTIAL FULL EMPLOYMENT BUDGET SURPLUS. MOREOVER, AUSTRALIAN BUDGETS HAVE MOVED PROGRESSIVELY IN PAST 3 YEARS FROM LARGE FULL EMPLOYMENT DEFICIT TO PRESENT POSITION OF SURPLUS. IN OTHER WORDS, IN MIDST OF RECESSION FISCAL POLICY HAS BECOME EVEN MORE RESTRICTIVE.

5. WHILE THERE IS NO QUESTION THAT FACTOR SHARES WERE ALTERED BY RAPID WAGE RUN-UP IN PRE-RECESSIONARY PERIOD, AND SHOULD BE RESTORED TO MORE NORMAL MAGNITUDES, EMBASSY BELIEVES THERE CAN BE LITTLE QUESTION THAT PROGRESSIVE TIGHTENING OF FISCAL POLICY HAS BEEN IN LARGE PART RESPONSIBLE FOR FORESTALLING AUSTRALIAN ECONOMIC RECOVERY.

6. WITH MONEY SUPPLY UNDER CONTROL AND UNDERUTILIZED PRODUCTIVE CAPACITY, THERE SEEMS LITTLE DOUBT THAT AUSTRALIAN FISCAL POLICY COULD MOVE FROM RESTRICTIVE TO NEUTRAL (I.E., FULL EMPLOYMENT BALANCED BUDGET) WITHOUT AGGRAVATING INFLATION.

7. WITH RESPECT TO FOREIGN SECTOR, EMBASSY BELIEVES AUSTRALIAN DOLLAR TO BE OVERVALUED AS CONSEQUENCE OF INFLATED DOMESTIC PRICE LEVEL AND LONG-TERM FALL-OFF IN INVESTMENT INFLOW. CONSEQUENCE OF OVERVALUATION IS TO LIMITED OFFICIAL USE

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INCREASE IMPORT PRESSURES ON MANY AUSTRALIAN PRODUCTS. MOREOVER, SLEEECTIVE INCREASE IN PROTECTION FOR PRODUCTS MOST SEVERELY AFFECTED BY IMPORT COMPETITION, E.G., AUTOMOBILES, TEXTILES, SHOES, HAS SHIFTED GREATER BURDEN ONTO LESS PROTECTED PRODUCTS. DESPITE THIS, HGHIHY PROTECTED INDUSTRIES CONTINUE TO BE DISTRESSED, IN SOME CASES BECAUSE THEY ARE ONLY marginally COMPETITIVE EVEN WITH INCREASED PROTECTION, AND IN SOME CASES BECAUSE DEMAND HAS DROPPED DUE TO HIGHER PRICES AND DOMESTIC RE-CESSION. AUTOMOBILES ARE CASE IN POINT, WITH SALES DOWN SHARPLY DESPITE INCREASED PROTECTION AND CHRYSLER AND GM REPORTING SUBSTANTIAL LOSSES FOR LAST YEAR.

8, THUS, IT IS ONLY A SLIGHT EXAGGERATION TO SAY THAT ALL OF AUSTRALIAN INDUSTRY IS FACED WITH SEVERE IMPORT COMPETITION.

9. UNFORTUNATELY, AN IMPORTANT PRPORTION OF THOSE RESPON-SIBLE (BOTH WITHIN GOVERNMENT AND INDUSTRY AND UNIONS) FOR THE MANAGEMENT OF AUSTRALIA'S MANUFACTURING SECTOR SEEM WEDDED TO THE CONVICTION THAT ONLY THROUGH INCREASED PRO-TECTION CAN THEIR OBVIOUSLY DISTRESSED INDUSTRIES BE SAVED

AND INDUSTRIAL EMPLOYMENT MAINTAINED. THIS VIEW IS NOT SHARED BY THE HIGHLY QUALIFIED ECONOMISTS IN AUSTRALIA'S INDUSTRIES ASSISTANCE COMMISSION, BY RURAL INTERESTS AND PRIMARY PRODUCERS, AND BY CONSUMERS AS A WHOLE,

INCREASED PROTECTION CAN BE CLEARLY SEEN BY THE OUTSIDE OBSERVER TO BE SELF-DEFEATING, AND UNDER PRESENT CONDITIONS IT IS PROBABLE THAT SELECTIVE DOMESTIC MEASURES TO SUSTAIN EMPLOYMENT IN INDUSTRY WILL NOT BY THEMSELVES BE ADEQUATE. IT IS FOR THIS REASON THAT EMBASSY CONCURS SO WHOLEHEARTEDLY IN MISSION'S JUDGMENT, AS EXPRESSED IN PARA 11 (A) OF REF A, THAT LESS RESTRICTIVE DEMAND MANAGEMENT POLICIES ARE TO BE PREFERRED.

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10. COMPREHENSIVE SOLUTION TO PROBLEMS OF AUSTRALIAN INDUSTRY ALSO DEPENDS, HOWEVER, ON INTRODUCTION OF A MORE REALISTIC EXCHANGE RATE. FLOATING OF AUSTRALIAN DOLLAR WOULD BE A HIGHLY DESIRABLE INITIAL STEP TOWARDS ACHIEVING THIS. REDUCTION OF PROTECTION ON MOST HIGHLY PROTECTED INDUSTRIES, SUCH AS AUTOMOBILES, WOULD BE A NECESSARY SECOND STEP, WITH EXCHANGE RATE USED AS EQUILIBRATING MECHANISM TO BRING PENT-UP IMPORT DEMAND INTO LINE WITH FOREIGN EXCHANGE AVAILABILITIES.

11. THOUGH COMPUTER ANALYSIS WOULD BE NECESSARY TO PROVE THE POINT, EMBASSY BELIEVES THAT THESE TWO MEASURES ALONE WOULD GO A LONG WAY TOWARD MAKING AUSTRALIAN INDUSTRY MORE

COMPETITIVE. DESIRABLE THIRD STEP AT SOME POINT WOULD OBVIOUSLY BE A GENERAL LOWERING OF AUSTRALIAN LEVELS OF PROTECTION, WITH EXCHANGE RATE CONTINUING TO PLAY ROLE OF EQUILIBRATING MECHANISM.

12. POTENTIAL FOR EXCHANGE RATE ADJUSTMENT TO FUNCTION AS AN ALTERNATIVE TO PROTECTIONISM REPRESENTS A TOTALLY ALIEN LIMITED OFFICIAL USE

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CONCEPT TO MOST AUSTRALIAN POLICYMAKERS. IT IS AN UPHILL BATTLE TRYING TO SELL THIS CONCEPT. NEVERLESS, IF U.S. MISSION CAN MAKE ANY HEADWAY, IT WILL BE OF GREAT BENEFIT BOTH TO AUSTRALIAN ECONOMY AND TO CAUSE OF WORLD TRADE. EMBASSY OFFERS ITS SUPPORT FOR U.S. MISSION EFFORTS IN THIS REGARD AND WISHES TO EXPRESS ITS APPRECIATION FOR HIGH DEGREE OF INTEREST AND EXPERTISE EMBODIED IN MISSION REPORTING AND ANALYSIS OF SECRETARIAT DOCUMENT. ALSTON

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